No. 11962

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

PROCTER & GAMBLE MANUFACTURING CO.,

Appellant,

vs.

H. F. METCALF, Trustee in Bankruptcy of the Estate of F. P. NEWPORT CORPORATION, LTD., Bankrupt, DOROTHY DAY, MARTHA McMILLEN, MATILDA OLSEN, WILLIAM H. NEBLETT, MRS. F. P. NEWPORT, EUGENE P. CLARK, F. P. NEWPORT CORPORATION, LTD., RUBY E. NEBLETT, SECURITY-FIRST NATIONAL BANK OF LOS ANGELES and JOSEPH SATTLER,

Appellees.

Reply Brief of Appellees, Dorothy Day, Martha McMillen, Matilda Olsen, William H. Neblett, Mrs. F. P. Newport, Eugene P. Clark, and F. P. Newport Corporation, Ltd.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Cases.

Statutes.

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Preliminary Statement.

Of the last named appellees, Dorothy Day, Martha McMillen, Matilda Olsen, William H. Neblett, Mrs. F. P. Newport and Eugene P. Clark, are unsecured creditors of the F. P. Newport Corporation, Ltd., the bankrupt corporation, and F. P. Newport Corporation, Ltd. is the said bankrupt.

Said unsecured creditors and the Bank of America National Trust and Savings Association were the subject of

Finding No. "11" included in the "Findings of Fact, Conclusions of Law and Order of the Referee" dated December 19, 1947, which is as follows:

> "That Dorothy Day, Martha McMillen, Matilda Olsen, William H. Neblett, Mrs. F. P. Newport, Eugene P. Clark and Bank of America have filed, in the bankruptcy proceedings herein, unsecured claims against the bankrupt corporation in the approximate sum of $140,000.00, which is approximately 70% of the unsecured claims so filed in this proceeding." [Tr. p. 29.]

Said unsecured creditors, on November 13, 1947, filed with the referee written objections to the proposed sale, and another unsecured creditor, Ruby E. Neblett, filed on said day separate written objections thereto.

When the matter of the proposed sale and of the objections thereto were first called for hearing on November 13, 1947, Bank of America National Trust and Savings Association appeared through its counsel, Edmund Nelson, Esq., and stated orally that it objected to said sale. [Tr. p. 77.] In reference of said written objections we find the following in said Findings of Fact, Conclusions of Law and Order:

> ". . . and Bank of America having, in open court, joined in said written objections . . ." [Tr. p. 27.]

Bank of America did not file a petition for a review of the referee's said Order, dated December 19, 1947, but said appellees and the bankrupt did, and at the hearing before the District Court on March 11, 1948, of the peti-

tion of said appellees to review said Order, the following took place:

> "Mr. Cahill: At this time Bank of America appears through its counsel and offers to aid the bankrupt and the creditors represented by myself in the prosecution of this petition for a review; and at this time I move your Honor that Mr. Edmund Nelson be associated as counsel with myself in this proceeding (5).
>
> "The Court: He may do so." [Tr. p. 313.]

Of the numerous persons interested in said proposed sale no appeal has been taken to this Court by said Bank or by any of the other secured creditors; nor by Security-First National Bank of Los Angeles, the secured creditor; nor by the trustee in bankruptcy; nor by the bankrupt; nor any of the unsecured creditors, from the Order of the District Court of May 10, 1948, entitled "Order vacating and setting aside referee's Order of December 19, 1947, *re* sale of Real Property to Procter & Gamble Manufacturing Company." The sole person appealing is the last named company, the proposed purchaser.

It is important to note also that Joseph Sattler, who has filed with this Court a document entitled "Memorandum on Appeal by Joseph Sattler, Appellee" wherein he prays "that the order of the lower court be reversed" *has not appealed from said order.* Said order as to him is a final order and it would appear that his said "memorandum" praying for reversal of an order that he has not appealed from should be stricken on that ground alone. There exists, however, an additional reason why said memorandum should be stricken and that is that totally unsupported allegations have been set forth therein, particu-

larly in paragraph "I", "II" and "III" thereof, which are not true, and in one instance is so serious as to be deemed by the bankrupt as being on the border line of libel. Claims of unsecured creditors actually in a sum in excess of $200,000.00 [Findings, par. 11; Tr. p. 29] are set forth in said memorandum as being "approximately less than $100,000.00 in amount" (Memorandum p. 2) and of total fees for referee, receiver, trustee, reporters, consultants and attorneys in the total sum of approximately $136,744.66, in an estate that has operated as a going concern over a long period of years with a gross income a few thousand dollars less than $2,000,000.00, of which said fees in excess of $75,000.00 remain unpaid, this Honorable Court is advised by said memorandum as to said unpaid amount as follows:

". . . some of which have not been paid." (Memo- p. 2.) (See *U. S. v. H. H. Metcalf,* as trustee, etc., 131 F. 2d 677, where this Honorable Court held that said trustee was conducting a business, and required to pay income taxes upon the profits therefrom.

Elsewhere herein reference will be made to the statement made in paragraph "III" of said memorandum that "the price of $198,000 . . . is all things considered, a very fair offer under the circumstances," which will be considered in the light of the following appearing in a letter certified by the referee to have been "written by Mr. Sattler . . . in an effort to sell the property . . ." [Tr. p. 67]:

> "If in the near future some understanding should be made between the oil company and the estate, *the price for this property, in private hands, might be quoted around a million dollars.*" [Tr. p. 86.] (Emphasis added.)

Statement of the Case.

The facts presented by appellant under the heading "Statement of the Case" have been limited to nine short sentences which take up less than one page of its opening brief. (App. Op. Br. p. 3.) Apart from said nine sentences this Honorable Court can only become advised as to the facts by either examining the Transcript of the Record, which is composed of 425 pages, or by considering such facts as are set forth by appellant in that part of its opening brief entitled "Argument."

The difficulty with the procedure last mentioned is that such facts as are there set forth are not only interspersed with appellant's contentions and its argument in reference to same; but are scattered throughout the various points set forth under the heading "Argument" over the remaining 36 pages of its opening brief.

Appellees feel, therefore, that it is incumbent upon them to set forth at this place a comprehensive recital of facts. They feel, also, that such procedure is necessary in the light of the fact that whatever factual recitals as have been made by appellant anywhere in its opening brief are such as tend primarily to bring into consideration the question of the adequacy of the price offered by appellant for the real property owned by the trustee in bankruptcy.

If "adequacy of price" were the sole or primary objection made by appellees to the proposed sale the matter would not be so serious. "Adequacy of price" having been neither the sole nor primary objection, and there having been a number of objections made by appellees in

reference to the detriment to other assets of the Estate through the unusual and extraordinary conditions appellant had attached to its offer of purchase, such objections should, in the opinion of appellees, be placed before this Honorable Court at the outset in their fullness, rather than as a matter of casual mention here and there throughout appellant's argument. It is believed that this Honorable Court will then more readily observe why the Judge of the United States District Court, after taking of additional testimony and listening to arguments of all interested parties over a period of two days [Tr. p. 91 to 94] and after reading "the entire transcript of the testimony before the referee" [Tr. pp. 92, 93]; and being undoubtedly profoundly shocked by what was revealed thereby; promptly set aside the order of the referee after first making, amongst others, this express finding:

> ". . . and that the terms and conditions imposed upon the trustee and the within Estate, by said Company, as terms and conditions of said sale, *were and are detrimental and injurious to the within Estate* and to the best interests of the creditors thereof; and it further appearing that the Referee was acting beyond his jurisdiction in ordering the payment of said real estate broker's commission, and in its payment *under the circumstances shown* would have been unauthorized, and contrary to law; and *that many of the objections presented in writing to the Referee* at the hearing before him *were serious objections that should have been sustained by him* . . ." [Tr. pp. 93-94.] (Emphasis added.)

THE FACTS.

The Trustee's Petition.

On October 27, 1947, F. P. Newport Corporation, Ltd., a corporation, was an adjudicated bankrupt [Tr. p. 5]; the Honorable Hugh L. Dickson was the qualified and acting referee to whom said matter had been assigned [Tr. p. 6] and H. F. Metcalf was the duly appointed, qualified and acting trustee in bankruptcy in said matter. [Tr. p. 7.]

That on said day said trustee filed with said referee his petition, in writing, for an order confirming sale of real property and praying that "notice of the hearing of this petition be given as required by law" [Tr. p. 10]; that "upon the hearing of said petition" [Tr. p. 10] an order be made approving the sale to appellant *"subject to the conditions set forth in the offer as hereinbefore set forth"* [Tr. p. 10] (emphasis added); that petitioner "be authorized to enter into a contract for the removal of tanks, poles, oil lines, sumps, etc., set forth in subdivision (d) of paragraph 4 of this opinion, in order to comply with the terms of said offer" [Tr. p. 10]; that he be authorized to pay to proceeds of the sale to the secured creditor upon it releasing its claim against said property by deed reserving ". . . unto the sellers all interest and rights, rents, royalties . . ." accruing to the said trustee as Lessor under an existing oil and gas lease upon the property involved [Tr. pp. 10-11] and that petitioner be authorized to "pay recording charges, escrow fees, title fees, internal

revenue stamps . . ." and other expenses, including "All expenses incurred by petitioner in the matter of removing all storage tanks . . ." etc. [Tr. p. 11.]

No authorization was sought for the payment of a real estate broker's commission and said petition did not set forth any statement or facts whatsoever upon that subject.

The lands described in said petition were by metes and bounds description which discloses that they are situate in the Long Beach Harbor area and have frontage of 500 feet on Channel No. 3 [Tr. p. 7], and said petition recited that appellant offered the sum of $198,000.00 for same, subject to the condition that the trustee vested title of said land in appellant, including "all minerals, oil, gas . . ." free and clear "but reserving and excepting unto said trustee in bankruptcy all rents, royalties, and other things of value accruing pursuant to and *prior to the expiration, surrender or other termination* of that certain oil and gas lease dated January 14, 1938, by and between said Trustee in Bankruptcy, *et al.,* and the Universal Consolidated Oil Company as Lessee . . ." [Tr. p. 8.] (Emphasis added.)

Said petition also, amongst other things, set forth that the estimated cost of removing said oil well tanks and equipment was "between $15,000 and $16,000." [Tr. p. 9.]

The Objections of Appellees and the Separate Objections of Bank of America National Trust and Savings Association and of Ruby Neblett.

Appellees, on November 13, 1947, filed with said referee their written objections to the proposed sale set forth in said petition.

Believing that the proposed sale was highly dangerous to the estate, because of the conditions attached to appellant's offer of purchase, and believing that a detriment would certainly affect the remaining assets of the estate because of such conditions, and that the loss resulting therefrom might equal or exceed the total sum offered by appellant; appellees included in said written objections the following:

"III.

"That the condition set forth in subparagraph '(b)' of paragraph '4' of said petition, that the trustee shall convey to the buyer 'all minerals, oil, gas and other hydrocarbon substances, in or produced upon said lands,' reserving only to the trustee the rents or royalties under the present lease with Universal Consolidated Oil Company, is not only inequitable and unjust and highly dangerous in a business sense as to the trustee, but will, as your objectors are informed and believe and for such reasons allege, operate to the detriment of the within estate and to their rights therein by causing a loss to the estate which may exceed in amount the total purchase price of $198,000.00 offered by the proposed purchaser, and in this regard objectors specify as follows:

"(a) That your objectors have been informed by thoroughly competent authorities, and they believe and for such reasons allege that because of the difference in value to royalty buyers be-

tween minerals, in places owned by the seller, and rents and royalties under a lease, that the value of the estate herein of its interest in the oil and gas yet to be (15) recovered from said lands, will drop fifty per cent (50%) immediately upon the transfer of said lands under said condition, and that said depreciation will take place solely because of said condition;

"(b) That in addition the within estate, under said condition, and notwithstanding said reservation will be in grave danger of taking an equally great loss by being deprived in the future of all rents and royalties, now being received by said trustee, through his present lease with the Universal Consolidated Oil Company. The reason is obvious. Universal Consolidated Oil Company has the right to abandon its lease with the trustee at any time by quitclaiming the demised premises to said trustee, or otherwise.

"If that were done today the trustee has a perfect legal right to lease said lands to other oil companies. It is common knowledge that in the Los Angeles Basin lands are frequently leased profitably after the original lessee-producer has abandoned his lease. The trustee would also have the right, following such abandonment or quitclaiming to enter upon the said lands and produce the wells now located thereon taking the entire production to himself.

"Both of said rights will be immediately lost to the trustee because of said condition.

"It is equally obvious, that the proposed purchaser could under said condition, with perfect legal right, approach said Universal Consolidated Oil Company the day after the proposed purchaser acquired title, as proposed, and offer to said Oil Company, any sum

from one dollar to a million dollars that it thought said Oil Company would accept, as an inducement to abandon its lease or (16) to quitclaim said described lands.

"And the day after that happened the purchaser could lease the same lands with perfect legal right to Universal Consolidated Oil, or to any other person, and the trustee would not only no longer have any interest in the oil and gas produced from said lands or the rents or royalties therefrom, but he would have no right to complain of any such transaction, because under said condition he not only leaves himself 'wide open' to the happening of such a transaction but, even through unintentionally, he almost invites it." [Tr. pp. 13-14-15.]

"IV.

"That said proposed offer of $198,000.00 is not in reality an offer in that sum for as set forth in subparagraph '(d)' of said paragraph '4' the proposed purchaser attaches still another condition to his offer and that is that the trustee shall pay all costs of moving 'all storage tanks, power poles, oil lines, sumps, steam (18) lines and concrete walls' (one concrete wall excepted) now located on said lands.

"That, in the opinion of your objectors this is an operation that said trustee should in no event engage in. It is apparent that if the trustee, while engaged in such operation, should cause loss of life, or damage to property through explosion, fire, flooding or for any other cause that the within estate might be held liable in damages in very great sums of money.

"In paragraph '5' of said petition the trustee states that he believes that the cost of removal can be limited to between $15,000 and $16,000. There is no assurance, however, that the estate will not actually pay

out double or treble those sums. Your objectors are informed and believe and for such reasons allege that the said trustee has until very recently estimated the cost of such removal at approximately $33,000.00." [Tr. p. 17.]

Other objections set forth therein were placed upon the ground that oil had been produced from the six acre parcel proposed to be sold to appellant, during the period of the trusteeship, of a total value of $1,341,363.04; all of which had been produced from oil sands overlying two lower sands known as "The Ford Zone" and the "237 Zone" which were producing profitably upon adjacent and adjoining lands from wells as to which it was alleged that one well was but a few hundred feet from the said six acre parcel; and that, while the said trustee had the right, absolutely, under his lease with Universal Oil Company, to produce or to cause others to produce from such sands in the event that said company elected not to produce oil therefrom, or quitclaim said lands, or abandon its lease; that the trustee's right to so produce upon the happening of one or all of said events would cease to exist *ipso facto* with the transfer of said six acre parcel to appellant under the conditions imposed by it. [Tr. pp. 15-16.]

Appellees' objection as to the inadequacy of price was set forth as follows:

"I.

"That the lands described in said petition have a fair market value in the sum of Four Hundred Thousand Dollars ($400,000.00) and the offer received by

the said trustee in the sum of $198,000.00 as reported in said petition, is an entirely inadequate price being less than one-half of the present fair market value of said (14) lands.

"II.

"That said lands were appraised, by a thoroughly competent appraiser, about a year ago, who rendered his report to the above named bankrupt herein, in furtherance of the reorganization plans of said bankrupt, wherein he stated that said lands had a fair market value in the sum of $391,386.60.

"That your objectors are informed and believe and for such reasons allege that because of the tremendous development program by the City of Long Beach, now under way in reference to this harbor, and for other well known reasons, that the fair market value of said lands has increased since said appraisal was made." [Tr. pp. 12-13.]

Further objection was made upon the grounds that the proposed sale was otherwise not to the best interest of the estate or to the creditors thereof and additional reasons were stated as follows:

"(a) That after the trustee shall deduct from said $198,000.00 the cost of removal of said tanks and equipment, and the commissions (if any) and the expenses of sale, and the Federal and State Income Taxes, necessarily arising from such sale which taxes cannot be definitely determined at this time because of the uncertainty as to the actual cost of removal of said tanks, and equipment, but which are substantial, the net sum remaining will be so small that the loss of this valuable six acres of waterfront property, coupled with the possible loss of all of the oil yet to be produced therefrom, will be entirely without justification; (19)

"(b) That the Debtor's ability to rehabilitate himself by a plan of reorganization, now under way with the aid and co-operation of a number of his important creditors, will in no way be aided by such an insignificant sum of money but will on the contrary be delayed and possibly defeated as shown in the next succeeding paragraph;

"(c) That if hereafter the said trustee as Lessor and Universal Consolidated Oil Company as Lessee desired to extend the term of said lease or to modify said lease for their mutual gain and advantage they would be totally unable to do so without the consent of said proposed purchaser, and it should be self-evident that such consent would be withheld. The legal question that arises under such consideration has possibly been decided in an oil and gas case by the Supreme Court of Oklahoma and the precise question has recently been placed before the California Supreme Court, which Court has referred the matter to the District Court of Appeal for the Fourth District for decision." [Tr. pp. 17-18.]

Said objectors concluded with a recital of proceedings in reference to a $400,000 loan and a $75,000 credit, as part of a plan of reorganization. [Tr. pp. 18-19-20.]

The written objections filed by Ruby E. Neblett, as the equitable owner of certain corporate stock of the bankrupt, after adopting the said objections of appellees [Tr. p. 21], set forth further objections as follows:

"2. The record does not indicate that a sufficient public advertisement of the sale of the property has been made to enlist the interest of proposed buyers able and willing to purchase land of the character proposed to be sold.

"3. The contemplated sale price of the property does not appear to be its fair market value in view of the statement of the Trustees herein, made by written communication to the referee herein, (24) dated July 2, 1947, to the effect that the Trustee was asking $374,000.00 for the Wilmington property.

"4. The terms of the sale, in imposing upon the Trustee the obligation to remove the obstruction upon the property, would create a possible liability for damages incurred in the operation and doubt may exist as to the extent of the power of the Trustee to engage in such operation." [Tr. p. 21.]

As hereinbefore stated, and as shown by the Findings of Fact made by the referee [Tr. pp. 26-35], Bank of America National Trust and Savings Association, ". . . a secured and unsecured creditor" [Tr. p. 26], appeared through its counsel, Edmund Nelson, Esq., and after examining the said written objections of appellees and of the said Ruby E. Neblett, ". . . in open court, joined in said written objections." [Tr. pp. 26-27.]

Security-First National Bank of Los Angeles, the secured creditor, appeared at said hearing and filed a memorandum stating its approval of the proposed sale, and stating that of the indebtedness of $1,351,729.38 due it on the day of adjudication of bankruptcy that all had been paid but the sum of $320,222.85 (thereby acknowledging the receipt from the trustee of principal payments alone in excess of $1,000,000.00) but complaining that during the year 1946 and during 1947 to the date of said hearing that it had been paid $83,485.58, of which somewhat less than one-half were from payments made by said trustee from his income from oil and the remainder from the disposal of other assets. [Tr. pp. 22-25.]

The Hearing Before the Referee.

On November 13, 1947, the first day of the hearing before the referee, appellees called HARVEY C. HIGGINS, who testified, in part, that he had been "Land appraiser for Southern Pacific Company . . . since 1922" [Tr. p. 100]; that he had been recently transferred to San Francisco ". . . to take over the land and appraising of the entire Southern Pacific Company" with the title "Engineer and Land Evaluation" [Tr. p. 100]; that since 1922 he had appraised ". . . over a hundred million dollars worth of property for said company, including waterfront lands at San Francisco, Oakland, Portland, San Pedro and Long Beach" [Tr. p. 101]; that he had also made appraisals of like property for A. T. S. F. Railway Company of the value of "about twenty million dollars" [Tr. p. 101]; that Southern Pacific Company was the owner of 31.86 acres of land adjoining said six acre parcel owned by the said trustee [Tr. p. 101]; that he had appraised said six acres on January 30, 1946, as having a value of $359,436.00 [Tr. p. 102]; that in his opinion that was the value of said parcel as of November 13, 1947 [Tr. p. 103]; that he had appraised said 31.86 acre parcel about six months before as having a value of ". . . $60,000.00 an acre (is) for surface rights only for industrial purposes" and did ". . . not include the minerals" [Tr. p. 104]; that said lands were the "same value" as those of the estate [Tr. p. 105] and that said appraisal of $359,436.00 was for "the surface rights only for industrial purposes" [Tr. p. 105] and did "not include minerals." [Tr. p. 105.]

Upon the second day of the hearing before the referee the said trustee, in open Court, offered said property for sale to the general public. [Tr. p. 112.]

Thereupon H. F. METCALF, the said trustee, testified, in part, as follows:

That he had received an offer from a construction company to perform the oil equipment removal required of him under one of the conditions of appellant's offer of purchase, for the sum of $20,378.00; that he had advertised the six acre parcel for sale in January, 1946 [Tr. p. 123]; that he had not advertised the property ". . . in regard to this proposed sale" [Tr. p. 124]; that he had placed an advertisement in a Long Beach paper during 1947 but that was ". . . six or eight months ago" [Tr. p. 124]; that he obtained results therefrom. [Tr. p. 124.]

During the course of Mr. Metcalf's testimony an appraisal previously made by Thomas J. Cunningham of said six acre parcel, in the sum of $211,462.00, was admitted in evidence by referee. [Tr. p. 117.] While it was being offered, some discussion took place as to when it was made, the referee recalling that it was "approximately a year ago" [Tr. p. 116]; L. M. Cahill, attorney for certain objectors, stated that "it will be about two years next January" [Tr. p. 117] and Mr. Lynch, attorney for the trustee, stating that the thought ". . . that the actual appraisal was made in December, 1945." [Tr. p. 117.]

Thereupon the following took place:

> "Mr. Cahill: Your Honor is advised written objections have been filed *in* (by) my office on behalf of certain creditors (26) of the bankrupt.
>
> Mr. Lynch: The burden of proof is on the parties objecting.
>
> Mr. Nelson: I would like to ask for a stipulation that the Bank of America may rely on the written objections filed by Mr. Cahill.

The Referee: You want to join in with them?
Mr. Nelson: Without filing separate objections.
Mr. Lynch: I have no objection." [Tr. p. 117.]

H. V. Johnson, called as an expert witness on behalf of appellees, testified that he had been an appraiser of lands and improvements thereon for 25 years [Tr. pp. 126-127]; that he had made important and extensive appraisals for Security-First National Bank of Los Angeles [Tr. pp. 126-127], for Building and Loan Associations [Tr. pp. 127-128], for Title Guarantee and Trust Company, as its chief appraiser for eleven years [Tr. p. 129], for the State of California [Tr. p. 131], for the United States Government [Tr. pp. 132-133], and for many others.

He stated that in his opinion the fair market value of the property was the sum of $419,571.00. [Tr. p. 134.]

Roy G. Mead, called as an expert on behalf of appellees, testified that he was a Consulting Engineer and Geologist; that he had been so engaged as such for 26 or 27 years after graduating from the University of Arizona, where he took honor degrees in geology and mining engineering [Tr. p. 163]; that for the past 25 years the major part of his work had been ". . . on oil geology in the various fields of California, and particularly in the Los Angeles Basin" [Tr. p. 163]; that he was familiar with the practice in producing oil wells and the practice in reference to the owner of the lands upon which oil wells are located [Tr. pp. 163-164]; that he had made appraisals of oil properties for numerous major and independent oil companies which he named [Tr. pp. 164-165], and for the United States Government as a field examiner

for the United States Land Office [Tr. p. 165]; that he had been employed by the United States Government within ". . . the last two or three years . . . on a case involving oil prices, in the Kettleman Hills oil field" [Tr. p. 165]; that he had been employed by the State of California [Tr. p. 165]; that he made appraisals for inheritance tax purposes ". . . both for the royalty owner and the operator" [Tr. p. 165], and that he was familiar with the said six acre parcel.

After a recital to him of certain of the pertinent facts of the proposed sale to appellant [Tr. p. 167], he was asked this question by counsel for appellee:

> "Having these facts in mind, I will ask you if, in your opinion, such a proposed sale with such reservation is regarded as sound practice on the part of the land owner." [Tr. p. 167.]

After objections were overruled, he replied as follows:

> "A. As I understand the question and the explanation, answering the question, *I would say it would not be, because the oil interest would be jeopardized and the owner of the property, who now has the property, would not get the oil rights after the expiration of the present lease.*" [Tr. pp. 167-168.] (Emphasis added.)

After some discussion, the following took place:

> "By Mr. Cahill:
>
> Q. That is the fact. That being the fact, what, in your opinion, is the danger of the Trustee in Bankruptcy in selling this asset in this manner? A. He would lose the protection that would run to the landowner in the event the lease was terminated.

Mr. Lynch: There is no question about that.

The Witness: *Therefore the value would be lower."* [Tr. p. 168.] (Emphasis added.)

"By Mr. Cahill:

Q. Because of that factor is it true that those who would purchase, and that a sale not having been made —the proposed sale—the interest in the oil from the Trustee, will they pay, in your opinion, a lesser figure if the sale is consummated on that basis?" [Tr. p. 168.]

Following some discussion between the referee and counsel, the question was explained as follows:

"Mr. Cahill: I will put it this way:

Q. The estate today has certain interests—*it is the owner of the minerals,* subject to a certain executed lease. If those minerals were offered on the market today they would bring a price, which we will indicate as X price. Now, query: If this sale is made so that the Seller, the Trustee in Bankruptcy, *no longer owns the minerals in place, but he simply owns an interest under an oil and gas lease, will the buyer* who would have today paid X price *be only willing to pay then* a day after the sale takes place, Y price, *presumably* a much lower price?" [Tr. p. 169.] (Emphasis added.)

After some further discussion, the referee said: "He can answer." [Tr. p. 169.] Mr. Mead then answered as follows:

"The Witness: Yes, I would say he would. It is a case where you are a direct royalty owner and after the sale there would be an over-riding royalty which would be affected by the lease." [Tr. p. 170.]

In an endeavor to establish the extent of the detriment caused thereby, the following questions were asked and the following answers given:

"By Mr. Cahill:

Q. In your opinion, would his selling price, over-riding royalty, be much lower than the interest we have today? A. Yes.

Q. Would you have any idea what percentage, approximately? A. Well, that would vary with conditions. It might be the same in some cases, and in other cases it might be 50 per cent lower. In order to tell exactly what that would be you would have to make an appraisal of the oil and ascertain how much oil would be recovered after the lease was terminated. I would say it would be, at least, 25 per cent less.

Q. In your opinion, the value the Trustee has today would be depreciated about 25 per cent through making this sale in the manner that it is proposed to be made with the reservation only as to our interest under the lease? A. That is just an opinion, but it could be verified (93) by an appraisal of the oil rights.

Q. Have you found in your experience that oil royalty buyers will pay less, substantially less, where what they are buying is only an over-riding royalty under a lease? A. No, they don't pay as much landowner royalty where lower rights run, when the land is more desirable than the over-riding royalty. That depends upon the terms of the contract.

Q. The reason why— A. The landowner royalty runs with the property. If a lease is terminated the landowner still has the mineral rights, and he can either operate the property himself or he can lease

again. In the case of over-riding royalty, when the lease terminates, that mineral right is lost and ceases to be.

Mr. Cahill: That is all." [Tr. pp. 170-171.]

Following Mr. Mead's testimony, considerable discussion took place before the referee in reference to obtaining the testimony of Mr. Albert A. Carrey, who had been called by appellee at an earlier day but who had not been heard and was absent from the district on the day that Mr. Mead testified. [Tr. pp. 172-173-174.] It was pointed out by Mr. Edmund Nelson, on behalf of objector Bank of America, that Mr. Carrey's testimony was of extreme importance for the reason (as stated by Mr. Nelson):

"Mr. Carrey has testified in this matter before, as a geologist, and he is the adviser of the Trustee which (he) had been through the proceeding. I think he is better informed than anyone else about the conditions here, geologically and otherwise." [Tr. p. 174.]

After further discussion it was decided to endeavor to have Mr. Carrey present on a subsequent day and that if he could not attend that a statement would be obtained from him in writing as to his opinion as to the proposed sale and that said statement would, by stipulation, be placed in evidence.

The initial testimony of Albert A. Carrey was presented to the referee on November 26, 1947, in the form of a letter which was, pursuant to stipulation, received in evidence. The stipulation was to the effect ". . . that if Mr. Carrey were called at (the) this time, sworn and testified as a witness, that he would testify as set forth in (the) this letter." [Tr. p. 195.] The letter so received

in evidence was on the printed stationery of "A. A. Carrey, Petroleum Geologist and Engineer," was dated November 17, 1947, and was as follows:

"Mr. L. M. Cahill, Attorney at Law,
"606 South Hill Street,
"Los Angeles, California.

"Dear Mr. Cahill:

"The petition of H. F. Metcalf, Trustee, for (120a) the sale to the Procter & Gamble Manufacturing Company of certain properties located within the Wilmington oil field has been brought to my attention. Said property is owned by the F. P. Newport Corporation and is at present leased and operated for oil by the Universal Consolidated Oil Company.

"I have been requested to study said petition and render any opinions that I might have insofar as said sale might affect the present and future economical operation of the wells now located on the property.

"I shall only attempt to base my opinion upon good oil field practice and the matter of operating leases. By way of qualification I might state that I have been actively interested in the oil business for 25 years, as a consulting petroleum geologist and engineer for 20 years, and more particularly I have been the field agent for the trustee, Mr. H. F. Metcalf, in connection with this particular property for approximately nine years.

"As a result of that experience I have had occasion to study the original lease many times and feel that I am familiar with the operations in so far as they affect this particular property. (121)

"From a study of paragraph B of the above-mentioned fee, it appears to me that the sale of this prop-

erty would change the present landowners' position in that the Newport Corporation would be the owners of a so-called 'over-riding royalty,' rather than as present they are the owners of the mineral interest. Said sale would in a sense convert present oil and gas lease into a restrictive lease, in which case the termination period would be of prime importance. Such a restricted lease might preclude the possibility of the Newport Corporation operating the wells themselves some time in the future.

"In explanation of the above statement, it will undoubtedly come to pass some time in the future that the present operating company might feel that it is no longer profitable for them to operate under said lease. In such cases it has been found that the fee owner can often operate such leases where an operating company, which has to pay high royalties, cannot do so.

"It is my opinion that if this sale is made that the present landowner, the F. P. Newport Corporation, will suffer a decided loss in the sale value of their landowner's interest. It has been my experience that there are few buyers (122) for over-riding royalties, as most royalty buyers prefer mineral interests. In each case where I have observed sales, it has been my experience that over-riding royalties always bring considerably smaller prices than landowner's royalties or mineral deeds.

"I believe that the most serious effect that the sale would have upon the F. P. Newport Corporation is in the matter of the termination clause in the present lease. If such a sale is made the F. P. Newport Corporation has no power to prevent the present operating company from terminating said lease, and as a result of such action the F. P. Newport Corporation could in no way continue the oil operations.

"In answer to paragraphs C and D, I do not believe that the changes in the physical equipment on the leases particularly work any hardships on an operating company. It may to some extent limit their freedom in the matter of remodeling work and the handling of oils from the various wells, but I do not believe it will be serious enough because too great inconvenience.

"Hoping the above information will be of some assistance in clearing up some of the points in connection with said sale, I remain, (123)

"Very truly yours,

"(Signed) A. A. CARREY."

Subsequently, A. A. CARREY was called as a witness and gave testimony on behalf of appellees and he stated in part as follows: that he was a consulting geologist, petroleum engineer, and that he also operated an oil company [Tr. p. 247]; that he had been so engaged since his graduation from Stanford University in the Department of Geology, in the year 1922 [Tr. p. 247]; that he had been employed by various oil companies as geologist or chief geologist and that for most of the time "for a company that is now the Texas Company" [Tr. p. 247]; that he had been employed by the said trustee in the Newport matter as petroleum engineer for a number of years and that he was thoroughly familiar with the oil wells upon said six acre parcel and with the production zones underlying same [Tr. pp. 248-249-250]; that in his opinion an unproduced oil zone, known as the "Ford Zone" existed beneath said six acre parcel [Tr. pp. 251-253-255]; that in his opinion a still lower and unproduced horizon existed beneath said six acre parcel, as to which there existed ". . . a fair chance of production." [Tr. p. 257.]

Roy G. Mead was recalled and gave further testimony. He stated that he was present at the hearing at which time Mr. Carrey testified and at the time that another expert, a Mr. Follansbee, testified. [Tr. p. 264.] The following then took place:

"By Mr. Cahill:

Q. After having heard the testimony of those two experts, do you remain of the opinion that as to this 6 acres, that the Ford Zone lies thereunder? [209] A. Yes, I am still of that opinion.

Q. And that there might be a possibility of profitable production from that zone? A. Yes, that is my opinion. I wouldn't know how much production, but there is a possibility of some production in my opinion.

Q. Do you also have an opinion at this time after having heard their testimony in reference to the possibility of production from the 237 Zone? A. I am of the opinion that the 237 Zone lies under this property as well as the Ford Zone.

Q. Do you think that the production might be profitable from that? A. It might be more profitable in the 237 Zone than the Ford Zone.

Q. Do you think that both those zones should be drilled in and tested by production tests? A. By all means I do." [Tr. pp. 264-265.]

Thomas F. Mason, produced by and on behalf of the secured creditor, testified: that he was a realtor and appraiser and had been so engaged since 1923 [Tr. p. 178]; that he had appraised property for the County of Los Angeles, State of California, United States Army, banks and others and that he had appraised much beach property in Los Angeles and Orange counties, including the hold-

ings of the Harbor Department of the City of Los Angeles [Tr. pp. 178-179]; and that in his opinion ". . . the fair market value of the surface rights only of the (this) property under discussion here is $196,350.00, as of the date of this trial." [Tr. pp. 178-179-180.]

G. F. Follansbee, Jr., the Vice President of said Universal Consolidated Oil Company, called as a witness for and on behalf of said trustee, testified as follows: that he was such officer of said oil company [Tr. p. 223]; that he was an engineer, having graduated from Stanford University with an A. B. in Geology, following which he took one year's graduate work in petroleum engineering [Tr. p. 223]; that he had been employed by the California State Division of Oil and Gas as an engineer and that he had been with said oil company 19 years as an engineer and geologist [Tr. p. 223]; that he was familiar with a deepening operation on one of the wells producing on said six acre parcel [Tr. p. 224]; that cores were taken and that ". . . there was some fair looking sand which we were undecided upon at the time" [Tr. p. 224]; that after giving the matter some consideration and "running the log" it was his opinion that a commercial well could not be obtained in that portion of the Ford Zone [Tr. p. 224]; that the well deepened had not at any time been a very good producer [Tr. p. 226]; that although the sand located in that portion of the Ford Zone ". . . was fair looking sand" [Tr. p. 227], that "no tests were run" [Tr. p. 233]; that the 237 Zone had not been discovered in the general area at the time of such drilling and that his company did not drill down to where it might have been [Tr. p. 233]; and that, following said deepening, ". . . there was no production test attempted of any kind either with or without casing." [Tr. p. 234.]

CLARK C. BURGESS, called as a witness on behalf of appellees, gave testimony as follows: that he was a realtor, so engaged at Long Beach, California, since 1934 [Tr. p. 238]; that he was familiar with waterfront property in that area and that he had recently been successful in negotiating leases of waterfront property in that area [Tr. pp. 238-239]; and that in his opinion the said six acre parcel, with which he was familiar, was salable ". . . in the neighborhood of some sixty to sixty-five thousand dollars an acre." [Tr. p. 240.]

F. P. NEWPORT, President of the bankrupt corporation, gave testimony as follows: that he was a real estate broker and appraiser and had been engaged as such in California for over 40 years [Tr. p. 278]; that he had made appraisals in the District Court of the United States and in the Superior Court of the State of California and that he was then acting as appraiser for the Federal Court, which was referred to as "Mr. Laugharn's court" [Tr. p. 278]; that he had purchased said six acre parcel on February 13, 1913 and had been familiar with it at all times since [Tr. pp. 278-279]; that he had been familiar with the sale of property, particularly water front property in the Long Beach harbor area, over a period of 30 years and that in his opinion the fair value of the surface rights of said six acre parcel was in the sum of $391,000.00 [Tr. p. 279]; that he had determined that he could obtain a loan from California Western States Life Insurance Company in the sum of $400,000.00 as part of a plan of reorganization [Tr. p. 281]; and a credit in the sum of $75,000.00 as part of said plan. [Tr. p. 283.]

R. T. Adams, Assistant Vice President of Security-First National Bank of Los Angeles, the secured creditor, called on behalf of said bank, gave testimony as to the balance of principal due to said bank. [Tr. pp. 287-289.]

J. B. Gribble, called as a witness on behalf of appellees, testified that he was the auditor employed by said trustee [Tr. p. 276]; that he had made a calculation that, after deducting the cost of removing the tanks and other equipment from said six acre parcel, which cost was in the sum of $20,378.00, that of the balance remaining after deducting said sum from the $198,000.00 price offered by appellant there would be left a sum as to which the trustee would be required to pay an income tax in the sum of $20,761.18. [Tr. pp. 276-277.]

The Order of the Referee.

On December 19, 1947, the referee made his order upon said petition and the said objections thereto. The order embodied certain findings, none of which were upon the issues raised by said petition and the objections thereto except the statement in the nature of a conclusion of law "that the objections, and each of them, made to said sale are without merit" [Tr. p. 29], and except a statement that a plan of reorganization had not been presented and that a loan of $500,000.00 would not be sufficient to pay the creditors of the estate plus the expenses of administration [Tr. p. 29] and except a brief recital in reference to the undeveloped oil zones, which was simply to the effect that ". . . it is not now known whether or not oil and gas could or can be produced in commercially profitable quantities . . ." [Tr. p. 29.]

The findings were silent as to the several issues raised that the proposed sale with the conditions demanded by appellant attached would be detrimental to the estate and cause tremendous loss and depreciation as to the remaining assets, and no finding was made whatsoever as to the fair market value of the property, the referee in that regard simply noting that the property had been appraised by ". . . Thomas Cunningham, appointed by this court for said purpose," at $211,462.00, without noting, however, the time that said appraisal was made. [Tr. p. 28.] As hereinbefore shown, the record discloses that Mr. Cunningham's appraisal had been made almost two years prior to the date of said findings.

On December 29, 1947, appellees filed with said referee their petition to review the referee's said order. That after a recital therein of the objections of appellees, of Bank of America National Trust & Savings Association, and of the said Ruby E. Neblett, appellees set forth in 12 subparagraphs of paragraph "IX" thereof their reasons why they believed that said order is erroneous. [Tr. pp. 41-46.] That said paragraphs constituted an assignment of errors which have been hereinafter referred to under point "IV" of the argument. As all of said paragraphs are fully set forth in the appendix attached hereto, they will not be further discussed at this place. Paragraph "XI" of said petition was as follows:

> "That no findings of any kind have been made upon the principal objections set forth in said written objections, your petitioners must therefore request that a transcript be prepared to include all matters received in evidence at said hearings, with the exception of the matters received by reference." [Tr. p. 27.]

Referee's Certificate on Review.

Said certificate was prepared prior to the completion of said transcript and reflects the difficulty, and almost the impossibility, of attempting to prepare from memory an accurate record of a summary of the evidence even though only a little over a month's time had elapsed following the hearing.

The Proceedings Before the District Court.

On March 11, 1948, transcript of the proceedings before the referee then being available, the District Judge announced during the course of the proceedings ". . . in any event I am going to have to go through this transcript" [Tr. p. 397], and the record discloses that shortly thereafter the following took place:

> "The Court: I have got to read this evidence. I have got to investigate this record made before the referee." [Tr. p. 397.]

Thereafter, and at the close of the hearing on that day, and after the Court had announced that the matter would be continued to April 26, 1948, the Court said:

> "I am going to read this record between now and then, even though I have a pretty good idea of what it is already. Following that we can then dispose of the matter." [Tr. p. 421.]

On March 19, 1948, the District Court made its order postponing the matter until April 26, 1948, for ". . . further consideration of said matter and the hearing of

further arguments therein" [Tr. p. 64] and for the purpose of considering any additional bids that might be received in the interim. [Tr. p. 64.]

The order which is appealed from hereunder was made on May 10, 1948. It embodied certain findings which the Court stated that it made after considering the further evidence placed before it and after examining and considering the said petition for review, the referee's certificate on review,, the amendment thereto, and the ". . . transcript of the record of the proceedings before the referee . . ." [Tr. p. 93.]

As to the danger of detriment and loss to the estate because of the conditions attached to said proposed sale to appellant, the Court found

> ". . . that the terms and conditions imposed upon the Trustee and upon the within Estate, by said Company, as terms and conditions of said sale, were and are detrimental and injurious to the within Estate and to the best interests of the creditors thereof . . ." [Tr. p. 93.]

As to the adequacy of the price offered by appellant, the Court said:

> ". . . that the consideration offered by said Procter & Gamble Manufacturing Company for said real estate in the sum of $198,000.00, less the cost of removing said oil well equipment, and payment of other costs and if allowed the payment of the alleged commission was a totally inadequate price for said real estate . . ." [Tr. p. 93.]

As to the payment of the real estate broker's commission in the sum of $5,000, the Court found

> ". . . that the referee was acting beyond his jurisdiction in ordering the payment of said real estate broker's commission and that its payment under the circumstances shown would have been unauthorized and contrary to law . . ." [Tr. pp. 93-94.]

Finally, the Court made a general finding

> ". . . that many of the objections presented in writing to the referee at the hearing before him were serious objections that should have been sustained by him, and that a confirmation of said sale should not have been made by the referee herein . . ." [Tr. pp. 93-94.]

Said order directed that the said order of the referee be reversed, vacated and set aside. [Tr. p. 94.]

ARGUMENT.

I.

The Order of the District Court Appealed From Was One in Its Discretion and Having Exercised That Discretion by Disapproving the Sale of the Property to Appellant, Such Order Should Not Be Reversed on Appeal.

That such is the rule readily appears from the decision in *Currin v. Nourse*, 8 Cir., 66 F. 2d 137, cert. denied 294 U. S. 729, where the court first states the reason for the rule as follows:

> "The approval of a sale of a bankrupt's property is peculiarly a matter for the court of bankruptcy, and one with respect to which this court should not and will not substitute its judgment for that of the lower court."

The court then proceeds to state the rule as follows:

> "An appellate court is precluded from revising the exercise of discretion in setting aside a judicial sale by a court having equitable jurisdiction, unless there is an abuse of power, or the case is in other respects extreme. *In re Shea* (C. C. A. 1), 126 Fed. 153, 156; *In re Wolke Lead Batteries Co.* (C. C. A. 6th), 294 Fed. 509, 511; *Century Motor Truck Co. v. Noyes* (C. C. A. 1), 18 Fed. 2d 546, 547. *The same rule would apply in the proper exercise of discretion in confirming a sale.*" (Emphasis added.)
>
> *Currin v. Nourse,* 8 Cir., 66 F. 2d 137.

II.

Appellant Has in Error Assumed That the Proposed Sale Was "Confirmed" by the Referee's Order, and That Thereafter the Rule Relative to the Stability of Judicial Sales and the Rule Relative to the Setting Aside of "Completed" Sales Only Upon Certain Grounds, Have Full Application.

Appellant relies upon the early case (1914) of *In re Burr Mfg. & Supply Co.* (C. C. A. 2), 217 Fed. 16 (Appellant's Op. Br. pp. 24, 25, 26) and cases which have followed the general rule stated therein, which rule has, however, been repeatedly held not to have application to the approval or disapproval of a sale in bankruptcy until, following action by the referee, the District Court acts upon the matter.

In *Reid v. King,* 4 Cir., 145 F. 2d 868, the Court, in effect refusing to follow the *Burr* case, said:

> "The courts have not always borne in mind the important distinction between setting aside a completed sale and refusing confirmation of a sale which has been made subject to the approval of the court. *Morrison v. Burnette,* 8 Cir., 154 Fed. 617, 624; *In re Burr Mfg. & Supply Co.,* 2 Cir., 217 Fed. 216, 219; and the importance of a substantial offer at an advanced price after a sale has taken place, but before it has been confirmed, has not always been recognized. For example, in *Sturgiss v. Corbin,* 4 Cir., 141 Fed. 1, the alleged inadequacy was so slight that the court would have been justified in confirming the sale without reference to the gross inadequacy rule."

The case of *Sturgiss v. Corbin* there distinguished is a case also relied upon by appellant. (See App. Op. Br. pp. 38 and 39.)

It has been held that the successful bidder, under circumstances such as shown here, is not a purchaser and is not even vested with an equitable title until the said is confirmed. We quote as follows:

> "While the highest bidder of property offered for sale by a trustee in bankruptcy is entitled to have his bid accepted by the trustee and reported for confirmation (*In re Williams,* 197 Fed. 1, 116 C. C. A. 523), yet he is not a purchaser, and is not vested thereby with even an equitable title in the property until the sale is confirmed." *In re Wolke Lead Batteries Co.,* 6 Cir., 294 Fed 509, 510.

III.

The District Court, as a Court of Bankruptcy, Was Vested With Discretion to Review and Reverse the Order of the Referee Confirming the Sale.

In declaring that rule the court, in *In re Wolke Lead Batteries Co.,* 6 Cir., 294 Fed. 509, 510, also refused to follow the *Burr* case and distinguished it as having no application to facts existing there, which facts, while not identical, are similar in many important aspects to those here. The court said:

> "After a judicial sale has been confirmed by the court, and the equitable title has thereby vested in the purchaser, public policy requires that there should

be stability in such sales, and that the same should not be set aside, except for reasons for which equity should set aside a sale between individuals. *In re Burr Mfg. & Supply Co.,* 217 Fed. 16, 113 C. C. A. 126. The facts disclosed by this record differ materially from the facts upon which the court based its opinion in *Re Burr Mfg. & Supply Co., supra.* In the latter case the District Court had approved and confirmed the sale, thereby vesting in the bidder an equitable title in the property. Some time later the District Court entered an order vacating its former order approving and confirming the sale.

"In the instant case *the order of the referee confirming the sale* to Haag *was subject, in due course of procedure, to review by the District Court. That court was vested with discretion to review and reverse the order of the referee in refusing to confirm the same.* The reversal by the District Court of the order and decree of the referee approving and confirming the sale to Haag left him in exactly the same situation in which he would have been placed if the referee had refused to confirm the sale.

"The District Court having exercised its discretion in that behalf, this court will not reverse, except for an abuse of discretion. *Bryant v. Stockhausen Co.* (C. C. A.), 271 Fed. 921."

In re Wolke Lead Batteries Co., 6 Cir., 294 Fed. 509, 511.

IV.

The Discretion Exercised by the District Court in Electing to Review and in Reviewing the Referee's Order Was Eminently Proper, Thoroughly Sound and Quite Necessary in Order to Protect the Estate From a Heavy and Needless Loss.

Of the numerous issues raised by the trustee's said petition and the objections thereto of appellees, Bank of America National Trust and Savings Association and the said Ruby E. Neblett, the referee, by his findings, did not decide any of them except, inferentially by the general finding in the nature of a legal conclusion: "That the objections, and each of them, made to said sale are without merit" [Tr. p. 29], and by a finding that ". . . it is not now known whether oil and gas could or can be produced in commercially profitable quantities from any undeveloped strata or zones which may underlie said real property" [Tr. p. 29], and a recital that a plan of reorganization had not been submitted, and that a loan of $500,000.00 would not be sufficient to pay both the creditors and the expenses of administration.

Upon the petition of appellees for review of the referee's order made upon such findings, the District Court was confronted with the fact that, in the absence of a specific finding as to the danger to the estate of the proposed sale because of the conditions attached to same by appellant, or of the impropriety of said sale because of the other grounds of objection made by appellees and others thereto, that it was necessary for it to take further evidence, to read the entire transcript, and to otherwise become fully advised in the premises, and, thereafter, to make appropriate findings. The District Court was at the outset unable to determine from the findings made by the referee even his conclusion

of the fair market value of said six acre parcel, although expert appraisers had testified for several days upon that matter. The referee in that regard only noted that the said six acre parcel had been appraised, by an appraiser appointed by the Court, as having a value in the sum of $211,462.00; but, by naming the appraiser, it became apparent, as shown by the discussion between the referee and counsel, when his appraisal was placed in evidence, that such appraisal was made at a time nearly two years earlier.

Possibly no argument made under this point can exceed in power appellees' Assignment of Errors presented to the District Court as a part of their Petition to Review the Referee's Order. By reference they are hereby made a part hereof and for the convenience of this Honorable Court paragraph "IX" of said Petition to Review, which paragraph contained all of said Assignment of Errors, has been printed in the appendix hereto.

The District Court, on the contrary, after receiving further evidence, made its order which, in part, recited that the Court having considered same, and examined the Petition to Review, the Referee's Certificate, the amendment thereto, "and having examined the transcript of the record of the proceedings before the Referee" [Tr. p. 93]; caused to be embodied in said order express findings upon the said matters found upon, if at all, only inferentially by the referee.

As to the danger to the estate and to its assets because of the conditions attached to said offer by appellant, the District Court found:

> ". . . that the terms and conditions imposed upon the Trustee and upon the within Estate, by said Company, as terms and conditions of said sale, *were and*

are detrimental and injurious to the within Estate and to the best interests of the creditors thereof . . ." [Tr. p. 93.] (Emphasis added.)

The testimony of witnesses Mead and Carrey fully sustain such finding and no evidence was offered or received to the contrary. Their testimony has been partially reviewed herein under the heading "Statement of the Case."

As to the adequacy of the price bid, the Court said:

". . . the consideration offered by said Procter & Gamble Manufacturing Company for said real estate in the sum of $198,000, less the cost of removing certain oil well equipment and payment of other costs and if allowed the payment of the alleged commission, *was a totally inadequate price for said real estate.*" [Tr. p. 93.] (Emphasis added.)

While the evidence was conflicting as to the value of the property, it is inescapably true that of all of the five experts who testified as to value, four were of the opinion that the property was worth from approximately 80% to approximately 100% more than the value placed by the fifth appraiser.

The evidence also disclosed that the offer was not an offer of $198,000.00 but actually an offer in an unknown sum—a sum that would be the balance remaining after the trustee engaged in the hazardous and expensive task of removing oil well tanks, pipe lines, and equipment at his own expense; and otherwise paying all of the things demanded of him by appellant as conditions attached to said offer, as alleged, of $198,000.00.

It appeared also that whatever the actual net sum turned out to be that it was subject, in effect, to another deduction for the payment of income taxes in a sum in excess of $20,000.00 on profit arising because of the fact that the property had been owned first by Mr. Newport and then by the bankrupt corporation for about 30 years and had greatly enhanced in value during that period.

One of the conditions imposed by appellant was that the trustee accept all cash. Most buyers are willing, even anxious, to buy for 30% or less down and give first lien paper for the balance. Such a transaction is treated so favorably by the Government that the taxpayer pays very much less income taxes.

As to the payment of a real estate broker's commission to a broker who had not been employed by the trustee and who had no knowledge whatsoever of his claim for a commission, the District Court found:

> ". . . that the Referee was acting beyond his jurisdiction in ordering the payment of said real estate broker's commission, and that its payment under the circumstances shown would have been unauthorized and contrary to law." [Tr. pp. 93-94.]

This matter will be discussed at some length under the next succeeding point.

The District Court also found generally

> ". . . that many of the objections presented in writing to the Referee were serious objections that should have been sustained by him . . ." [Tr. p. 94.]

V.

It Is No Longer the Law That Confirmation of a Sale in Bankruptcy Should Not Be Refused Unless the Inadequacy of Price Alleged Is So Great as to Constitute a Fraud or Shock the Conscience, or Unless Accompanied by Unfairness, in at Least Some Slight Degree, by the Purchaser.

What appears to be the latest comprehensive statement in this regard is found in *Reid v. King,* 4 Cir., 157 F. 2d 868, 870, 871, from which we now quote as follows:

> "We are urged to reject these conclusions on the ground that confirmation of a judicial sale, even in bankruptcy, should not be refused for inadequacy of price, unless the price is so grossly inadequate as to raise a presumption of fraud or shock the conscience, or unless the inadequacy is great and is accompanied by circumstances of unfairness on the part of the party benefited. Authorities in this circuit and elsewhere are cited in support of the rule: *Sturgiss v. Corbin,* 4 Cir., 141 F. 1 (denial of confirmation on appeal reversed); *Jacobsohn v. Larkey,* 3 Cir., 245 F. 538, L. R. A. 1918C, 1176 (denial of confirmation on appeal affirmed); see also *Speers Sand & Clay Works v. American Trust Co.,* 4 Cir., 52 F. 2d 831, 835; *In re Yost & Cook,* 6 Cir., 70 F. 2d 614; *American Trading & Production Corp. v. Connor,* 4 Cir., 109 F. 2d 871; 6 Remington on Bankruptcy, 4th ed. sec. 2555.
>
> "It should be noted, however, that the phrase 'gross inadequacy' is of early origin and derives its authority from the procedure developed by the courts to govern execution sales and judicial sales so as to protect the interests of the parties, and especially to give stability to the sales and to encourage purchasers to bid with confidence. Kleber's Void Judicial and Execution Sales sec. 355. The rule has been taken

over by courts of bankruptcy under a statute whose prime purpose is to dispose of the assets of the bankrupt at the highest prices obtainable in the interest of the creditors; and not infrequently the conflict between this purpose and the need to inspire confidence in sales under the supervision of the court has given rise to uncertainties which are reflected in the decisions. The courts have not always borne in mind the important distinction between setting aside a completed sale and refusing confirmation of a sale which has been made subject to the approval of the court, *Morrison v. Burnette,* 8 Cir., 154 F. 617, 624; *In re Burr Mfg. & Supply Co.,* 2 Cir., 217 F. 16, 19; and the importance of a substantial offer at an advanced price after a sale has taken place, but before it has been confirmed, has not always been recognized. For example, in *Sturgiss v. Corbin,* 4 Cir., 141 F. 1, the alleged inadequacy was so slight that the court would have been justified in confirming the sale without reference to the gross inadequacy rule.

"The result is that some inconsistency is found in the statement of the rule in reported cases, and the courts in notable instances have departed from strict adherence in the interests of the creditors, even in the absence of unfairness or impropriety in the conduct of a sale, when the trustee has received a reliable and substantial advance bid after the sale has been held. In these cases the courts have accepted such an advance bid as sufficient without the accompaniment of those 'slight circumstances of unfairness' which in the earlier cases, such as *Morrison v. Burnette* and *In re Burr Mfg. & Supply Co., supra,* were thought necessary to justify a rejection of confirmation. . . .

"The case before us does not relate to the setting aside of a completed sale but to the confirmation of a sale made subject to the court's approval. The

concrete problem is whether or not the bidding should be reopened to let in a substantially higher bid. We see no reason why the court in this situation should not be permitted to exercise the authority granted it by the express terms of the statute to approve or disapprove the lower bid; or why the review of its decision on the point should not be limited by the rule which commits such decisions to the sound discretion of the court. *In re Hagerstown Silk Co.,* 4 Cir., 69 F. 2d 790; *In re Wolke Lead Batteries Co.,* 6 Cir., 294 F. 509; *In re Shea,* 1 Cir., 126 F. 153. This course, in our judgment, will produce more satisfactory results than a strict adherence to a verbal rule of thumb devised long ago to govern sales in another field." *Reid v. King,* 4 Cir., 156 F. 2d 868, 871.

VI.

The Referee Was Without Authority to Order the Payment of a Real Estate Broker's Fee as the Broker Had at No Time Been Employed by the Trustee but Was, on the Contrary, a "Finder" Rendering Service on Behalf of Appellant.

While it is apparent that the broker had an oral agreement with the referee [Tr. p. 290] the indisputable fact remains that the trustee did not employ him; did not know that he was rendering services [Tr. pp. 290-291], and the broker did not have an agreement in writing for the payment of a commission, as required by section 1624, Civil Code of the State of California.

Nothing could be clearer from the record.

Creditors knew nothing of the matter until the referee announced his oral decision in open court after the submitting of the issues raised by the trustee's petition and the said objections thereto. No notice of any such claim was given to creditors by either the trustee or the referee. The said petition of the trustee was completely silent as to any such matter [Tr. pp. 7-11]; and he testified in the presence of the broker as follows:

> "Mr. Metcalf: This man has never talked to me about this deal." [Tr. p. 291.]

The trustee's quoted statement had been preceded by the statement of his attorney that follows:

> "Mr. Lynch: I am not sure what the answer is, but Mr. Metcalf has not made any agreement or arrangement with anyone for the payment of any commission." [Tr. p. 290.]

And, at the same time and in the presence of said broker, appellant through its attorney, Richard C. Bergen, made the following statement:

> "Proctor and Gamble Representative: He was the finder and we have handled the negotiations from that point." [Tr. p. 290.]

The assignment of error in reference to this matter set forth in the Petition to Review the Referee's Order, is set forth in full in the appendix herein under subparagraph "(k)." Reference is made to it and it is made a part hereof as if fully set forth here. (Appendix p. 4.)

Appellant states in his opening brief, at page 16:

> "While we recognize Joseph Sattler as a 'finder' and think that the Referee had discretion to order the payment of a commission to him [Tr. p. 34], it is not a matter with which we are primarily concerned. Of course, if Judge Cavanagh had thought or this court thinks that the commission cannot properly be paid it is a matter for modification and not reversal." (App. Op. Br. p. 16.)

It is quite clear that the referee has no such discretion. Research on that point discloses the following:

> The referee is an office of the court exercising *judicial* functions. *In re Owl Drug Co.,* 16 Fed. Supp. 139.
>
> The referee is merely an officer of the court of bankruptcy. *Realty Associates etc. v. O'Connor,* 295 U. S. 295, 79 L. Ed. 1446.
>
> A referee has *no power* not conferred by the order of reference, by law or by general orders. *Weidhorn v. Levy,* 253 U. S. 268, 64 L. Ed. 898; *In re Faerstein,* C. C. A. 9th, 58 Fed. 2d 942; *In re Continental Producing Co.,* 261 Fed. 627; *In re Fox West Coast Theatres* (D. C. Cal.), 25 Fed. Supp. 250, affd. 9th Cir.; cert. denied U. S. Supreme Court; *Heiser v. Woodruff,* 150 Fed. 2d 867, cert. denied 326 U. S. 778.
>
> A referee has no authority to collect or receive money belonging to a bankrupt estate. *In re Pierce,* 111 Fed. 516.

VII.

Creditors Are Entitled to Notice of a Claim for a Brokerage Commission.

"Moreover, the petition for the order of sale ought to have apprised the court specifically of the claim for brokerage commission." *In re Grimm,* 35 Fed. Supp. 15, 17.

The court, in the *Grimm* case also declared:

"It is to be noted that General Order 45, 11 U. S. C. A. following section 53, provides: 'No auctioneer . . . shall be employed by a receiver, trustee or debtor in possession except upon an order of the court expressly fixing the amount of the compensation or the rate or measure thereof. . . .' Although the foregoing relates to public sales, *no reason appears why private real estate brokers should constitute a more favored class.* The policy of the law underlying General Order 45 would seem equally applicable to the circumstances existing in the present case."

Elsewhere the court said:

"The lien creditors were entitled to notice, before their assent to the sale was obtained, of the employment of a real estate broker and his claim for a commission from the proceeds. *Gold v. Southside Trust Co.,* 3 Cir. 1910, 179 Fed. 210, 213; Cert. denied, 1910, 218 U. S. 671. This was a relevant circumstance which might have affected their approval of the sale." *In re Grimm,* 35 Fed. Supp. 15, 17.

Joseph Sattler, the broker claiming a commission, is licensed as such under the laws of the State of California [Tr. p. 291] and he is, as such broker, subject to the laws of the State of California, as is the trustee. Section 1624 Civil Code of the State of California is in part as follows:

> "1624. What contracts must be written. *The following contracts are invalid,* unless the same, or some note or memorandum thereof is in writing subscribed by the party to be charged or by his agent:
>
> "5. An agreement authorizing or employing an agent or broker to purchase or sell real estate for compensation or a commission."

Appellant has possibly accepted statements such as the following, appearing in the several letters forwarded to it by the said "finder," as not being "puffing" but as being representations of substantial facts:

(a) "Should then this piece of harbor land revert to private ownership, the bid that you formerly presented for this piece, I hardly believe, would be considered for the three acre piece nearby." [Tr. p. 86.]

(b) "If in the near future some understanding should be made between the oil company and the estate, *the price for this property, in private hands,* might be quoted around a million dollars." [Tr. p. 86.]

(c) "If your factory management committee would reconsider this situation *you would be the owners of a very valuable piece* of ground underpriced." [Tr. p. 82.] (Emphasis added.)

If appellant believes those statements, it has an adequate remedy and that is to acquire the property from the trustee under a new offer, divorced from the present onerous conditons and at a price that would still be a "bargain" after a substantial increase of its present offer.

If, on the other hand, appellant does not believe said statements, and believes that it is not getting a bargain, it cannot be hurt by not acquiring property that had a value only in a sum equal to its offer.

Conclusion.

In the light of the Law and of the Facts, as stated, and because of the reasons herein set forth, the Order of the District Court should not be disturbed.

Dated: November 9, 1948.

Respectfully submitted,

LAWRENCE M. CAHILL,
Attorney for Appellees Dorothy Day, et al.

APPENDIX.

Paragraph IX of Petition to Review Referee's Order Containing Assingment of Errors.

IX.

That said order was and is erroneous in that:

(a) It, in effect, overrules and denies all of the said objections, notwithstanding that the evidence presented and received in support of said objections not only fully supported and sustained said objections, but was practically uncontradicted as to all matters set forth in said objections with the single exception of the question of present fair market value;

(b) That it authorizes the sale by the Trustee, over the written objections of possibly a great majority of the creditors, of a valuable asset of the within estate at a grossly inadequate price, believed by your petitioner to be approximately one-half of the fair market value of said six acre parcel, which belief is supported by the testimony of the Witness Higgins, who, as Chief valuation engineer, for Southern Pacific Company, placed a value of $60,000 per acre upon said six-acre parcel, same being exactly the value his company had placed upon its adjourning lands which he held to be exactly comparable;

(c) That it authorizes the sale upon the terms demanded by the purchaser in reference to the transfer of the mineral rights, whereby the trustee, being no longer the owner of the minerals in place, but having only a royalty interest therein expressly limited to the present lease, will become immediately subject to the possibility of immediate and complete loss of the

remaining oil and gas, not only as to the present producing sands, but also as to the said productive lower sands;

(d) That said proposed sale is unwise in this, that it changes a sound business and legal relationship now existing, as to oil and gas remaining to be recovered from said lands, into an uncertain one subject not only in a certain sense, to the whim or caprice of the present lessee, but subject also to the facts that upon any day after the sale, either for a small or large consideration paid by the proposed buyer to the present lessee, or for no consideration whatsoever so paid, the Trustee can be fully and finally divested of all remaining interest in the oil and gas from said lands by the present lessee simply informing the Trustee that he has quitclaimed said lands, as authorized in said lease, or, that he has abandoned said lease in its entirety;

(e) That all of the testimony as to present fair market value has been ignored but said order is predicated upon findings that notes only an appraisal made in either December 1945, or January 1946, whereas all of the testimony as to present fair market value disclosed that all lands in the Long Beach Harbor area have greatly increased in the two year period that followed said appraisal;

(f) That the trustee admitted that he has not advertised the property for sale in any manner, except a brief notice in the Los Angeles Daily Journal, notwithstanding the fact, that when he did extensively advertise said property for sale in January 1945, in

newspapers in various large cities upon both coasts, that he received, in the then not nearly so favorable market, numerous inquiries from corporations, brokers and others;

(g) That as late as July 2, 1947, the trustee believed that a buyer could be secured for said six acre parcel in the sum of $374,000.00, for as shown by the evidence he wrote the Referee herein, on that day, to that effiect;

(h) That as shown by the uncontradicted evidence, the trustee will be required, under the drastic terms of sale imposed by the buyer, not only to assume the risk of damage to person and property through fire, explosion, or otherwise, through the removing of the oil tank farm equipment to lands not proposed to be sold at this time but also to pay from the funds of the within Estate the minimum sum of $20,378.00 for such removal;

(i) That it ignores the recommendation of A. A. Carrey, who has been the petroleum geologist and engineer advising the Trustee herein, as to the oil and gas upon said lands, for a number of years; that the said lands not to be sold upon the drastic terms imposed by the buyer, as to the transfer of the mineral rights, because an immediate loss will be suffered by the Estate in the depreciation of the market value of the mineral rights. The uncontradicted testimony of Mr. Carrey on this point is in part as follows:

"In my opinion that if this sale is made that the present landowner the F. P. Newport Corporation, will suffer a decided loss in the sale value of their landowner's interest";

(j) That it ignores the recommendation of Mr. Carrey that the sale be not made for an entirely different reason stated by him as follows:

"I believe that the most serious effect that the sale would have upon the F. P. Newport Corporation is the matter of the termination clause in the present lease. If such a sale is made the F. P. Newport Corporation has not power to prevent the present operating company from terminating said lease, and as a result of such action the F. P. Newport Corporation could in no way continue the oil operations."

(k) That it directs the payment of an alleged real estate brokers commission in the sum of $5,000 to an attorney at law, who is apparently also licensed as a real estate broker, notwithstanding the fact that said attorney was at no time employed by the trustee herein in any capacity, attorney, broker or otherwise, and that it appears from the uncontradicted testimony that said attorney and the proposed purchaser entered into an agreement, without the knowledge of the trustee, that said attorney would be paid a "finders fee." As such this obligation would appear to be that of the party found and not the obligation of the trustee who had no agreement in writing, as required by the laws of the State of California, with any person for his employment as a broker, or otherwise or at all.

In this regard it should be noted that the trustee herein is a licensed real estate broker, who is allowed fees from time to time for his services as trustee herein, including $3,000 allowed him on December 23, 1947, for services rendered in 1947, and, that the record herein discloses that said trustee, about the month of January 1945, received an offer of purchase from the present proposed purchaser, for the same six acre parcel, in the sum of $180,000, which offer the trustee declined, he then having a higher offer; and that thereafter said attorney-broker conferred with the Referee herein and asked if a commission would be paid him if he was successful in finding a purchaser for said land; and that the Referee expressed an opinion that a commission would be paid because of the fact that he did not recall of sales of real estate being made before him where some real estate broker was not paid a commission; and that thereupon the said attorney wrote a letter to the corporation whose offer had been so declined by the trustee herein, and finding a continuing interest in the property upon its part here thereupon entered into said agreement for a "finders fee." The practice of buyers employing agents to secure scarce merchandise, or to induce reluctant owners to sell real estate, has developed in this period of scarcity, but the fee to be paid therefor is a fee to be paid by the buyer for whom the service is rendered, and is never a burden to be imposed upon the seller. In

any event such fees are not contemplated by the provisions of the National Bankruptcy Act and cannot be sustained and most certainly not under the circumstances here;

(l) That creditors herein have received no notice whatsoever as required by law of a hearing of a petition for the allowance to said attorney-broker of either a real estate commission or a "finder fee." The petition filed by the trustee herein failed to request authority to pay any such commission or fee to any person whomsoever and the notice thereof to creditors stated only the facts set forth in said petition.